ID 200415

November 17, 2000

BY HAND

The Honorable Vernon A. Williams, Secretary
Surface Transportation Board
Office of the Secretary
Case Control Unit
Attn: STB Ex Parte No. 582 (Sub-No. 1)
1925 K Street, NW
Washington, DC 20423-0001

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Re: STB Ex Parte No. 582 (Sub-No. 1),
"Major Rail Consolidation Procedures"

Dear Secretary Williams:

Enclosed for filing in the above-referenced matter are an original and 25 copies of the Opening Comments of CSX Corporation and CSX Transportation, Inc., together with a WordPerfect diskette. A certificate of service accompanies the document.

Kindly date-stamp the extra copy of this letter and the Comments, which our messenger is presenting, and return them to the messenger.

If there are any questions concerning this matter, please call the undersigned at (202) 942-5858.

Sincerely yours,

Dennis G. Lyons
Counsel for CSX Corporation and CSX Transportation, Inc.

rjm
Enclosures
cc All Parties of Record

BEFORE THE
SURFACE TRANSPORTATION BOARD

STB Ex Parte No. 582 (Sub-No. 1)

MAJOR RAIL CONSOLIDATION PROCEDURES

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November 17, 2000

TABLE OF CONTENTS

BEFORE THE
SURFACE TRANSPORTATION BOARD

STB Ex Parte No. 582 (Sub-No. 1)

MAJOR RAIL CONSOLIDATION PROCEDURES

OPENING COMMENTS OF CSX CORPORATION AND CSX TRANSPORTATION, INC.

Pursuant to the Board's Notice of Proposed Rulemaking ("NPR") served October 3, 2000, CSX Corporation and CSX Transportation, Inc., submit these Opening Comments on the proposed rules governing major rail consolidations set forth in the NPR.[1]

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1 We will refer to the Advance Notice of Proposed Rulemaking served March 30, 2000, as "ANPR." CSX Corporation and CSX Transportation, Inc. will collectively be referred to as "CSX." Conventional abbreviations will be used for other carriers. The existing railroad consolidation regulations found in Part 1180 of Title 49 C.F.R. will be referred to by the section numbers in Title 49 without repetition of the identification of that Title. The regulations proposed in the NPR will be referred to as "Proposed § 1180.x" as identified in the NPR. "Merger" and "Consolidation" will be used interchangeably to refer not only to statutory mergers and consolidations, but to other forms of combination of substantially all the properties of two rail carriers into a common control.

SUMMARY

In the NPR, the Board outlined a number of sound positions respecting major rail mergers. The Board correctly abandoned the outdated provision of the old Statement of General Policy for major rail consolidations that adopted as the principal goal of rail merger policy the elimination of redundant rail infrastructure. In its place, and in tune with the dynamic changes that have taken place in the industry, the Board appropriately now focuses its attention on the impact of mergers on inter- and intramodal competition and their effect on the United States transportation system and its economy.

Market-driven competitiveness is the proper focus of rail merger policy. The reliance on market forces engendered by the Staggers Act leads to the increased optimization of rail networks, to the benefit of railroads and shippers alike. The Board should promote market-driven competition, not increased regulation. Thus the Board has been correct to reject decisively proposals by some commenters that merger review and oversight proceedings be made an occasion to effect a reregulation of the industry. We strongly support positions taken by the Board to avoid forced access concessions. Those positions would recognize and protect the fundamental reality that railroads are networks, dependent on their long haul to compete with other modes and to generate the revenues necessary to meet

current obligations and the capital demands for renewal of their equipment and infrastructure.

There are, however, fundamental flaws in the manner in which the NPR articulates or applies the Statement of General Policy. While the Board properly has rejected the earlier presumption in favor of major rail mergers based on elimination of redundancy, language included in the NPR improperly suggests there may be a reverse presumption that would weigh against any future rail mergers. There exists neither an adequate factual nor theoretical foundation upon which to conclude that any and all future mergers likely will produce anticompetitive effects and/or implementation costs that will outweigh the benefits of those mergers. Moreover, such apparent antagonism toward mergers would put the Board at odds with all other regulatory agencies charged with the review of mergers.

To presume all mergers to be contrary to the public interest is unwarranted, and so therefore is any presumption that places on the parties proposing a merger some obligation to come forward with "competitive enhancements" to render a proposed merger acceptable. The NPR nonetheless seems to suggest just such a negative presumption. This, in turn, seems to have lead the Board to suggest that parties to a rail merger should seek to generate offsetting "procompetitive enhancements" of an unspecified amount and to unspecified parties. This troubling notion, which invites calls for an unwarranted alteration and dismantling of efficient rail operating networks, is compounded by the Board's apparent view that these "enhancements" need not, and probably will not, have any direct relationship to the putative harms allegedly flowing from a proposed merger.

CSX believes that the Board should begin its analysis, as do other federal agencies charged with merger review, with a more neutral view and examine each proposed merger on its own merits. The analysis should follow well-established methodologies for the analysis of the consumer welfare effects of proposed mergers. Efficiencies, such as those achieved from extended hauls, from the elimination of interchanges and from reduced costs and other service improvements, along with elimination of remaining inefficient redundancy, should be included among the procompetitive impacts of a proposed merger. In contrast, the NPR appears to treat such efficiencies separate from the competitive analysis. Anticompetitive concerns likewise carefully should be assessed under established and accepted standards, focusing on the impact of the proposed merger on competition and consumers, and not on competitors.

CSX also strongly urges that the Board's rules be crafted to shorten significantly the time consumed by the Board's review processes. The protracted review currently envisioned would increase uncertainty and would lead to inefficiencies that will reduce the benefits to shippers of a procompetitive merger.

CSX also believes that the Board's very correct conclusion that service assurance planning must be included in every rail merger proposal is somewhat compromised by the Board's apparent view that such planning is a static matter rather than a process.

Finally, a proposal by the Board to revise its treatment of voting trusts clearly will burden rail-to-rail mergers and compromise the effective and necessary system of separation of finance from control that the Board has developed through those voting trusts. It also will have adverse effects on the effectuation of rail-to-rail mergers as compared to unregulated acquisitions of major rail carriers.

These points and others are developed in what follows.

I. THE BOARD HAS PROPOSED A NUMBER OF SOUND POLICIES IN THE NOTICE OF PROPOSED RULEMAKING

A. The Board Has Correctly Focused the Public Interest Standard for Class I Rail Mergers on Competition

The Board correctly has chosen to remove the particular presumption, embodied in the existing policy statement, § 1180.1, that favors the approval of Class I rail mergers based on elimination of redundant facilities. The Board also correctly has chosen to replace that outdated policy with one that "seeks to ensure balanced and sustainable competition." The proposed revision to § 1180.1 properly recognizes that while "mergers of Class I railroads may advance our nation's economic growth and competitiveness through the provision of more efficient and responsive transportation," these procompetitive benefits, if adequately demonstrated, must be balanced against any reduction of rail or other competitive transportation alternatives resulting from the proposed merger. The Board properly recognizes that competitive considerations should play an important role in Board determination of any further proposed consolidation.

Market-based competition in transportation services benefits shippers, consumers, the rail industry and the nation. It is essential. Under proposed § 1180.1, the Board properly recognizes that certain reductions in the number of rail alternatives available to an individual shipper, absent other adequate competitive alternatives or countervailing enhancement to rail service, would not be in the public interest. The proposed policy statement properly identifies, as its ultimate goal, sustaining market based competition in the rail industry and explains the need for the new rules to focus the consolidation criteria on the level of "effective competition."

The new language in Proposed § 1180.1(c) expressly requires that any benefits, such as enhanced service and the creation of more efficient rail service providers shown to be likely to result from a merger, must be balanced against any service disruptions and any decrease in the number of transportation alternatives that are shown to be likely to result from the merger. The proposed policy statement also correctly recognizes that it is possible that certain procompetitive efficiency benefits of the sort that can be achieved through mergers likely are achievable through joint marketing arrangements, interline partnerships and other alliances between transportation providers. Alternatives of this type would not result in a permanent restructuring of the rail industry nor engender service disruptions that have the potential to reduce the procompetitive benefits of rail mergers, and thus, if subject to the Board's jurisdiction, should be made subject to exemption or an expedited process of review.

Many of the changes proposed by the Board to be made to the general statement of the public interest standard for reviewing mergers are, in CSX's view, generally sound and will promote only those mergers that are likely to produce service-enhancing efficiencies to the benefit of shippers and the nation's transportation system overall.

B. The Proposed Rules Properly Embrace the Board's Role of Ensuring that Future Class I Mergers Benefit Shippers, the U.S. Transportation System and Economy Generally

The proposed rules properly recognize that potential benefits from an end-to-end merger include both an improvement to existing competition, as well as new competitive opportunities, such as cheaper and/or better long-haul service that will benefit shippers. Under the new rules, these benefits must be weighed against any reduction of interline choices at major gateways post-merger. Moreover, the new rules require the consideration of the likely competitive response to the newly created, more efficient long-haul service. For example, if the likely response would be the creation of an alternative, equally efficient long-haul service through merger (or otherwise), the new rules require the consideration of how the two mergers (or merger and other response), taken together, would affect the overall public interest, *i.e.*, consideration of the level of competition that would result between the two more efficient long-haul service providers.

The proposed rules recognize that the next Class I merger may necessitate a response by the other railroads, making it appropriate that the merger be considered in light of its reasonably likely downstream effects. Those downstream effects include the potential benefits and harms of the applicants' merger in light of foreseeable subsequent mergers and other reactions. Moreover, the Board's stated willingness to consider the whole slate of public benefits in reviewing a merger is consistent with and required by the Board's governing statute.

C. The Board Very Wisely Chose Not to Seek to Reregulate the Rail Industry Via Merger Conditions

Consistent with the Staggers Act, the new rules reject reregulation of the rail industry through forced access or other intervention by the Board, and continue to allow the shippers, consumers and the rail industry to enjoy the benefits of market-based competition. These short-sighted proposals, which were put forward by a number of interest groups, are contrary to the long-term viability and competitiveness of the railroad industry. By promulgating merger rules that continue to allow appropriate procompetitive mergers, without the imposition of forced access merger conditions, the Board facilitates the free market forces that will continue to produce post-Staggers public benefits.

As previously explained in CSX's Reply Comments to the ANPR, forced access measures, though they may have certain short-run benefits to specific shippers, are, in the final analysis, regulatory handouts that constitute an abuse of regulatory discretion. Moreover, such reregulation through use of conditioning powers goes beyond public interest balancing and is in direct contravention of the governing legislation. The Staggers Act — and the Board and its predecessor's rejection of the anticompetitive DT&I conditions — removed regulatory barriers that had prevented railroads from competing in the marketplace on the basis of long haul and other efficiencies. The new rules, therefore, properly reject broad regulatory reshaping of the industry.

As CSX explained in detail in its earlier Reply Comments on the ANR, broad forced access relief, including forced switching or trackage rights, abandonment of the one-lump theory, or abandonment of the *Bottleneck* Rule essentially would cripple the industry and destroy the benefits of deregulation brought about through enactment of the Staggers Act. Since Staggers, shippers, consumers, and the rail industry have benefited from reduced rates and increased inter- and intramodal service. Market-based competition since Staggers has produced increases in lengths of haul and of productivity measured in terms of ton-miles per employee. Operating ratios have generally decreased, which has enabled lower rates and increased capital investment. Through its new rules, the Board should seek to continue to promote these benefits by rejecting forced access handouts, and embracing market-driven competition.

Indeed merger conditions that would require forced access have the potential for producing some of the very anticompetitive conditions that were sought to be corrected by the Staggers Act. For example, to the extent that forced access conditions are placed only upon the applicants, and granted only to some shippers and not others, they likely would result in an uneven, artificial, and inefficient competitive landscape. Such a result not only could potentially undermine smooth merger integration, but would create disincentives to invest in rail infrastructure or to pursue service-enhancing merger opportunities in the first place. Forced access merger conditions would undermine merger efficiencies, and would, in effect, subsidize less efficient competitors.

Imposing forced access in the context of an ongoing integration plan's execution would complicate substantially the applicants' ability to predict and manage an already complicated process. Trackage rights and new forced switching would introduce additional movements on rail lines, within terminals, and in yards themselves – all reducing available capacity needed to implement the merger. Subjecting applicants to these kinds of new operating obligations would create scheduling and asset allocation issues at precisely the most difficult operating period. The difficulties in integrating the merging railroads would be further complicated by having also to implement forced trackage rights and switching with railroads outside the merger that potentially will lead to service disruptions that will harm shippers.

Forced access merger conditions undermine market-based competition by replacing efficiency-enhancing competition with inefficiency-creating reregulation. Forced access remedies result in a subsidy to inefficient carriers at the expense of the efficiencies created by the merger. It is unlikely that such a forced access subsidy itself has any long-term efficiency-enhancing benefits. It would, in fact, create inefficiencies. Rather than creating more competition, forced access merely creates more competitors offering less attractive service. Such forced access handouts in many respects replicate the principal vice of the discredited DT&I conditions — they prevent or hamper the fulfillment of the procompetitive potentials of the transaction. Forced access merger conditions would require the Board to replace market-driven competition with inefficient reregulation in contravention of the basic deregulatory purpose of the Staggers Act.

While clearly rejecting most of the forced access proposals, the Board's Proposal is less clear on the "open gateways" urged by many commenting parties.[2] While this may appeal to some interests, the Board should recognize that broad open gateway requirements are the core of the failed DT&I conditions that were replete with anticompetitive effects and inefficiencies.

An unbounded open gateways requirement like the other forced access proposals would undermine network operations, adversely affect long-haul train densities, and reduce railroad incentives to invest in capital infrastructure that

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2 Proposed § 1180.1(c)(2)(i).

avoid the "equalization of rates" and "commercial closing" doctrines that were the most virulently anticompetitive features of those conditions.

The proposed new rules achieve a proper balance between specific shipper concerns that any additional consolidation not facilitate the exaction of noncompetitive rates and that any conditions imposed on such a merger not thwart the achievement of efficient rail services, which will benefit shippers overall.

D. The New Rules Properly Require Consideration of Cross-Border Effects in Merger Analysis

1. General

Recognizing that cross-border merger proposals may be anticipated, and that U.S. rail systems compete with rail systems in Canada, the new rules facilitate the Board's necessary consideration of cross-border effects as part of its merger analysis. Full-system analyses are necessary in order to evaluate rail systems that act as networks. Without full-system analysis, the Board will be denied the data necessary to understand impacts on competition, service, safety, labor, and the environment. A rule that neglects the evaluation of data of any part of that network because it lies across a political border would be totally ineffective.

Consideration of a major transnational system also raises novel jurisdiction, national interest, and national defense issues. The new rules properly require the applicants to address how safety concerns will be addressed in cooperation with benefits the industry and consumers. Were merging parties required to part with property or other legal rights unrelated to potential harms stemming from their contemplated merger, disincentives for efficiency-enhancing mergers would be created. The proposals made by some commenters in the filings responsive to the ANPR either sought to make mergers impossible or to create with a series of building blocks a reregulated industry. The Board did well to reject them.

While apparently flirting with concepts from the discredited DT&I conditions, the new rules wisely stop short of requiring applicants to perpetuate preexisting routes at every premerger interchange location. The new rules, rather, would require merger applicants to indicate how they will preserve the use of "major" gateways. (Proposed § 1180.6(b)(10).) Major gateways should be defined as the "well-established" transcontinental gateways (East-West) and similar well-established gateways North-South. If so limited, the adverse impacts of the rule may be minimized and some transitional benefits may be realized. The movements to be kept open should be specific as to duration, commodity, route, origin, and termination of substantial movements that afforded both originating and terminating carriers a long haul and were heavily used during the period prior to the filing of the Notice of Intent. These limitations are necessary if the Board is to avoid resurrection of the DT&I conditions. Moreover, any gateway provision must the Federal Railroad Administration. (Proposed §1180.1(k).) The new rules also permit the Board to consider the effect of the merger on the mobilization of the U.S. military. (Proposed § 1180.1(l).) The new rules properly require that applicants inform the Board where a merger will result in foreign control. This is significant because commercial decisions exercised post-merger could be based on foreign economic interests or on regulations that may differ from U.S. rail policy goals as established in the Staggers Act.

Moreover, issues involving foreign law, such as the ability of the transaction presented to the Board to be altered by the act of a foreign sovereign, need to be understood and factored into the merger analysis. The "Transnational Issues" section of the Policy Statement, Proposed § 1180.1(k), thus brings realism into the approach to mergers and consolidations involving as an applicant a railroad that has substantial operations in Canada or Mexico. The Board has quite properly not followed the advice of those who would ignore the issue and who have claimed that treaty arrangements such as NAFTA and the WTO arrangements — inevitably named but generally without citation to specific support — displace all of the Board's important concerns and its role in dealing with those issues. Those treaties clearly do not displace the Board.

2. Refinements

Some textual improvements in the proposal appear to be in order and to be consistent with, and indeed would effectuate the principles already set forth in the NPR. CSX's suggestions follow:

(1) At the end of the subparagraph 1 of Proposed § 1180.1(k), reference is made to how "ownership restrictions imposed by foreign governments" might affect the "public interest assessment." In addition to "ownership restrictions" that are "imposed by foreign governments," the Board must consider "directorship restrictions," some "imposed by foreign governments" but also some others simply imposed by the transaction documents. It is significant to note that not all such restrictions are imposed by foreign governments. Some are imposed simply by the parties to the transaction. It will be recalled that in the proposed CN/BNSF transaction, Finance Docket No. 33842, and later abandoned, there was "stapled share" arrangements under which not only would <u>CN</u> be governed by directors, a majority of whom were required by Canadian law to be residents of Canada (the shareholders of CN were apparently U.S. interests in a majority), but that the transaction documents required that the Delaware-incorporated holding company proposed to hold the stock of <u>BNSF</u> have a majority of Canadian residents as its

directors.[3] This requirement was imposed by the transaction documents apparently for tax or other reasons; Canadian law did not impose Canadianization upon BNSF's holding company, nor certainly did the Delaware General Corporation Law, which provides for no nationality or residence requirements whatsoever for the directors of a Delaware corporation.

The point is not just a peculiarity of a now-abandoned transaction. Because the CN/BNSF arrangements were apparently undertaken for private purposes and not to comply with Canadian law in respect of BNSF, it may well be that similar restrictions will reappear in transborder transactions involving those carriers or others. Accordingly, we respectfully suggest that the appropriate reference instead of "any ownership restrictions imposed by foreign governments" should be "any ownership, directorship or similar nationality or residence restrictions imposed by foreign governments or otherwise provided for in connection with the transaction."

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3 For the status of North American Railways, Inc, ("NAR"), the holding company involved, see the chart published by CN on its website and attached as an exhibit to UP-2, Finance Docket No. 33842, *CN et al.—Burlington Northern Santa Fe Corp. – Common Control*, at 13 and Ex. 1, filed March 1, 2000. For the requirement that the directors of NAR (also known as "Newco") be, in majority, Canadian residents, see the Cooperation Agreement among CN, NAR, BNSF, *et al.*, § 1.2, p. 2, as filed with the SEC as Exhibit 2.1 to Burlington Northern Santa Fe Corp.'s 8-K Report, File No. 1-11535, dated December 18, 1999.

(2) The Board quite rightly demands a "full system" competitive analysis and operating plan in transborder cases. Proposed § 1180.1(k). Presumably the required service assurance plans are to be presented on a system-wide basis since a breakdown in any node of a system may cause breakdowns elsewhere. So if the Board thinks it necessary, some explicit reference in Proposed § 1180.10 might be made, to avoid assertions that except for the subjects expressly mentioned in § 1180.1(k), matters outside the United States need not be discussed.[4] Moreover, while a full system application should be required, the rules should make it plain, either in Proposed § 1180.1(k) or throughout Proposed §§ 1180.6 through 1180.10, that the transborder materials need to be sufficiently separated in the full system presentations from the domestic data so that a public interest determination based on the public interest of the United States may be made. This point is made in the discussion of operational data proposed in § 1180.9 (at p. 34) which makes the point that the effect of the transaction "on the United States as a whole" is to be indicated. This treatment might well be extended throughout the provisions in the remainder of Proposed §§ 1180.6 through 1180.10.

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4 We note that while the second sentence of Proposed § 1180.1(k) seems to omit reference to service assurance plans, the proper point is made throughout Proposed §§ 1180.6 to 1180.9.

In this regard, a consistent reference to the transportation interests of the United States needs to be adopted. The "general" part of the proposed revised Policy Statement, Proposed § 1180.1(a), very correctly identifies a "broader transportation infrastructure that also embraces the nation's highways, waterways, ports and airports." Yet in Proposed § 1180.1(k), reference is simply made to the possibility of "actions that might be detrimental to the interest of the United States rail network." Presumably a broader reference was intended, such as "detrimental to the interests of the United States transportation network."

(3) Finally, in a related matter, the proposed definition of "applicant" excludes wholly owned direct or indirect subsidiaries of an applicant if the subsidiary is not a rail carrier. *See* Proposed § 1180.3(b). This exclusion, routinely granted under the existing rules on petitions for waiver in the case of purely domestic transactions, has some shortcomings when applied to transnational cases. Downstream holding companies can be used as the vehicle for foreign control (at the stockholder or director levels) of a United States-based railroad. A somewhat similar situation was involved in the CN/BNSF proposed transaction; a Delaware holding company was, through a contractual restriction as to its directors so that they were majority Canadian, to be the point of insurance of foreign control

over BNSF; the holding company with these director restrictions in turn was to hold the stock of the BNSF rail carrier or of its present holding company.[5]

Unless the Board is convinced that its powers over downstream holding companies that do not become "applicants" are sufficient to deal with that situation, there should be an exception in the rule for downstream holding companies that (i) are subject to or the source of ownership, directorship, or similar restrictions rela' d to nationality or residence, and (ii) are to control directly or indirectly one or more rail carriers operating within the United States.

II. AREAS WHERE THE PROPOSED RULES SHOULD BE CLARIFIED OR REVISED

As noted above, the NPR properly focuses the public interest standard on market-driven competition. In certain other respects, however, the document is flawed. We discuss these flaws next.

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5 *See* the discussion in CSX-2, Finance Docket No. 33842, *CN et al.—Burlington Northern Santa Fe Corp.—Common Control*, at 14-17 (filed March 1, 2000). CN/BNSF sought a waiver excluding the Delaware holding company from the definition then in effect. *Id.* CSX opposed that waiver, *id.*; in reply, CN/BNSF withdrew the requested waiver, BN/CN-10, Finance Docket No. 33842, *supra*, at 25-26 (filed March 6, 2000).

A. Broadly Accepted Standards of Competition Analysis Recognize that Procompetitive Effects of a Merger Should Be Balanced Against Anticompetitive Effects without Presumptions Pro or Con

The Board's Proposed § 1180.1, though setting forth the correct public interest standard, suggests that, when reviewing a proposed merger between Class I carriers, the Board would begin with the presumption that the merger likely would produce a not insignificant amount of unremediable competitive harm. Applying the correct public interest standard — but leaping beyond evidence or established economic theory — the Board suggests not simply the discarding but the reversal of the current presumption in favor of mergers: "the Board believes additional consolidation in the industry is . . . likely to result in a number of anticompetitive effects, such as loss of geographic competition, that are increasingly difficult to remedy directly or proportionately." *See* Proposed § 1180.1(c).

CSX believes that such a presumption is unsupported, unwarranted and would represent poor merger policy. Any mergers that emerge from the marketplace should rise or fall on their own merits. They may no longer enjoy a presumption; they may start at square one; they should not start in the hole of prejudgment.

1. Presuming Unremediable Competitive Harm Is Not Warranted and Is Inappropriate

A presumption that mergers harm competition, first of all, is inconsistent with the analytical frameworks employed by virtually all other federal agencies empowered by Congress to protect and regulate competition. The *Merger Guidelines* employed by the Department of Justice and the Federal Trade Commission do not create an up-front presumption that mergers either harm or benefit competition. They instead simply set forth an objective methodology for analyzing each proposed merger on a case-by-case basis, once the necessary facts have been collected.[6] The Federal Energy Regulatory Commission revised its merger policy in 1996, with the result that it now focuses more heavily on competition than it did in the past.[7] FERC chose not to incorporate an up-front presumption that mergers harm or benefit competition. In fact, it expressly adopted the DOJ/FTC *Merger Guidelines*, and its objective approach, as the FERC framework for analyzing the competitive effects of mergers.[8] The Federal Communications Commission, in its review of mergers among common carriers,

6 *See* U.S. Department of Justice and Federal Trade Commission, *Horizontal Merger Guidelines* §§ 0.1, 0.2 (issued 1992 and rev. 1997), *reprinted* 4 Trade Reg. Rep. (CCH) ¶ 13,104.

7 *See* Inquiry Concerning the Commission's Merger Policy under the Federal Power Act, 61 Fed. Reg. 68,595 (Dec. 30, 1996).

8 *See id.* at 68,596.

does not presume that consolidations cause competitive harm, but instead "use[s] a framework for competitive analysis" that is "embodied in the antitrust laws, including the [DOJ/FTC *Merger Guidelines*]."[9] Finally, the Department of Transportation, which retains significant authority over consolidations of U.S. and foreign air carriers, does not presume that consolidations cause competitive harm. In line with the Board, the Department of Transportation also "expect[s] the expansion of cooperative arrangements [between U.S. and foreign air carriers] to be largely beneficial . . . ."[10] These policies regarding both mergers and less integrative alliances benefit both applicants and their customers, because, by using more objective standards, likelihoods — both good and bad — are more easily analyzed and quantified, thereby enhancing the predictability of the merger review process. Predictability fosters less disruption to ongoing businesses and permits applicants to evaluate the prospects of a successful merger review process, avoiding mergers that would fail to be in the public interest.

The second reason the Board should not presume that further consolidation will cause unremediable competitive harm is that future consolidation among

9 *In re NYNEX Corp.–and–Bell Atlantic Corp.*, 12 F.C.C.R. 19985, ¶ 37 (1997).

10 Statement of United States International Air Transportation Policy, 60 Fed. Reg. 21,841, 21,843 (May 3, 1995).

Class I carriers is likely, in whole or in large part, to involve end-to-end combinations of carriers that generally do not compete against one another. End-to-end combinations, as compared to combinations of head-to-head competitors, hold greater promise of producing certain types of public benefits, such as new single-line service alternatives with longer hauls, more reliable service, and reduced interchange and terminal delays.[11] This principle is at the heart of the DOT's favorable predisposition toward consolidations among U.S. and foreign air carriers, which are primarily end-to-end in nature. In addition, as the Board recently reaffirmed, consistent with widely adopted economic principles, that end-to-end combinations "rarely result in a diminution of competition. [The Board has] adopted a presumption, known as the one-lump theory, that vertical combinations will not result in competitive harm."[12]

The Board's proposed presumption against further consolidation, even that which is largely or entirely end-to-end in nature, would have foreseeable and practical detrimental effects. The Board inappropriately may invite third parties to propose the imposition of self-serving conditions that are not needed to remedy

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11 *See, e.g.*, *Canadian Nat'l Ry. Co.—Control—Illinois Central Corp.*, Finance Docket No. 33556, Decision No. 37, slip op. at 22-23 (served May 25, 1999).

12 *CSX Corp., et al.—Control and Operating Leases/Agreements—Conrail Inc.*, Finance Docket No. 33388, Decision No. 89, slip op. at 49 (served July 23, 1998); *see also Western Resources, Inc. v. STB*, 109 F.3d 782 (D.C. Cir. 1997).

potential transaction-related competitive harms. Like the proposals in this rulemaking proceeding for sweeping reregulation of the industry through use of the Board's conditioning powers, Board articulation of unwarranted presumptions invite future concocted complaints.[13] Increasing the expectations of such interests would encumber and tend to discourage mergers that otherwise would be in the public interest. The uncertainties in the amount of tribute to be exacted would likely act as a *de facto* prohibition on mergers. The Board was wise not to adopt proposals for across-the-board reregulation via conditions. In the same vein, the Board would be wise not to adopt a presumption against mergers, which might be viewed as a signal that it is open to reregulatory conditioning on a case-by-case basis.

2. Cost Savings and Efficiencies Are an Integral Piece of the Competition Analysis

The Board's proposed revisions could be read to suggest that the efficiencies promised by a merger among Class I railroads are separate and distinct from applicants' proposals for "enhanced competition." "To offset harms that would not otherwise be mitigated," the Board would require "applicants [to] explain how the transaction and conditions they propose will enhance competition." Proposed

13 Discouraging such concocted complaints would tend to avoid calls that the Board's rules create what former Vice Chairman Owen has called "a Christmas

§ 1180.1(c)(2)(iv); *see also* Proposed § 1180.1(c) ("merger applications must include provisions for enhanced competition"). The Board's commentary suggests that its conception of proposals for "enhanced competition" more accurately might be described as proposals to benefit *competitors*, whether they benefit competition or not.

> Competition can be enhanced in many ways and we do not want to limit the approaches that could be proposed to enhance competition here. The focus of such a plan for enhancing competition could be placed on enhancing intramodal, or rail-to-rail, competition, for example, the granting of trackage rights, the establishment of shared or joint access areas, the removal of "paper" and "steel" barriers, and other techniques that would preserve and enhance railroad competition.

NPR, at 13. Despite the stated and clearly correct intention of "not want[ing] to limit the approaches that could be proposed to enhance competition," the Board's chosen examples suggest that it may not consider increased carrier efficiency a form of "enhanced competition" even through it permits the carrier to compete more strongly against other rail carriers or against other modes.

A conception of "enhanced competition" that fails to recognize increased rail carrier efficiency — promotive of inter- and intramodal competition — as a competitive benefit would not only logically be incomplete but would be

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tree," where parties could line up with contrived "concerns" for which they might demand mitigating conditions.

inconsistent with the analytical frameworks employed by other federal agencies responsible for protecting competition. The DOJ/FTC *Merger Guidelines*, which explicitly were adopted by FERC and cited favorably by the FCC, treat efficiencies as enhancements to competition, which must be evaluated side-by-side with any potential competitive harms.

> Efficiencies generated through merger can enhance the merged firm's ability and incentive to compete, which may result in lower prices, improved quality, enhanced service, or new products. . . .
>
> The Agency will not challenge a merger if cognizable efficiencies are of a character and magnitude such that the merger is not likely to be anticompetitive in any relevant market. To make the requisite determination, the Agency considers whether cognizable efficiencies likely would be sufficient to reverse the merger's potential to harm consumers in the relevant market, e.g., by preventing price increases in that market.[14]

In addition, DOJ, in its comments to the Board in merger proceedings, regularly recognizes that efficiencies arising from railroad mergers should be treated as enhancements to competition and weighed against any potential harm to competition.[15] DOT similarly recognizes that merger-related efficiencies are

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14 U.S. Department of Justice and Federal Trade Commission, *Horizontal Merger Guidelines* § 4.0 (issued 1992 and rev. 1997) (footnote omitted), *reprinted* 4 Trade Reg. Rep. (CCH) ¶ 13,104. "Cognizable efficiencies" are specific to the merger, have been verified, and "do not arise from anticompetitive reductions in output or service." *Id.*

15 *See, e.g.*, *Burlington Northern, Inc.—Control and Merger—Santa Fe Pac. Corp.*, Finance Docket No. 32549, Comments of the U.S. Department of Justice,

competitive enhancements, which must be evaluated right along with the potential competitive harms, in order to predict the competitive effects of a proposed transaction.

> Increased international code sharing and other cooperative arrangements can benefit consumers by increasing service options and *enhancing competition* between carriers, particularly for traffic to or from cities behind major gateways.[16]

The consistent treatment of efficiencies as competitive enhancements by DOJ, FTC, FERC, FCC, and DOT strongly suggests that the Board ought to be clear that its conception of "enhanced competition" is not limited to benefits to competitors. Merger applicants ought to be permitted, within the framework of

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May 10, 1995, at 7 ("the [Board] must balance the harm to competition against the merger's realistically expected public benefits and to include, as do the Merger Guidelines, the likely procompetitive efficiencies of the merger"); *Union Pac. Corp.—Control and Merger—Southern Pac. Rail Corp.*, Finance Docket No. 32760, Brief of the U.S. Department of Justice, June 3, 1996, at 42 ("Applicants have not sustained their burden of proving that there are 'substantial and demonstrable benefits to the transaction' that outweigh the far-reaching competitive harms described above.").

16 Statement of United States International Air Transportation Policy, 60 Fed. Reg. 21,841, 21,842 (May 3, 1995) (emphasis supplied); *see also* Joint Application of Delta Air Lines, Inc. et al. for approval of and Antitrust Immunity for Alliance Agreement, DOT Docket No. OST-95-618, Order 96-6-33, 1996 DOT Av. LEXIS 384, at *22 (DOT issued June 14, 1996) ("[T]he integration of the four carriers' services will, on balance, enhance competition in transatlantic markets and allow the airlines to provide better service and enable them to operate more efficiently; and it is unlikely that the Alliance Agreements, subject to certain conditions, will substantially reduce competition in any relevant market.").

Proposed § 1180.1(c)(2)(iv), to make proposals for "enhanced competition" that rely primarily, even exclusively, on increased carrier efficiency as demonstrating procompetitiveness and indeed offsetting potential harms.

Moreover, the Board ought to be explicit in its recognition that proposals for "enhanced competition" properly may include all types of merger-related efficiencies. These include enhancements to current service offerings (*e.g.*, end-to-end long-haul services), as well as cost savings from the elimination of redundancy.[17] To be sure, CSX cannot disagree with the Board's observation that "redundant capacity is no longer the issue it once was . . . ." Notice of Proposed Rulemaking, at 12. Future mergers among Class I railroads likely would involve carriers with few competitive overlaps, and thus, likely would lessen those types of cost savings. While cost savings from the elimination of redundant capacity generally might be expected to be smaller in the future, any savings that do materialize still would benefit shippers by decreasing the cost of service on a per-unit basis, which provides powerful incentive to lower rates, increase output, and

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17 Among the "efficiency gains" the Board regularly considers are cost reductions, cost savings, service improvements, economies of scale, scope, and density, elimination of interchanges, internal reroutes, more efficient movements between the merging parties, reduced overhead, and elimination of duplicative facilities. *See Canadian National Ry. Co.—Control—Illinois Central Corp.*, Finance Docket No. 33556, Decision No. 37, slip op. at 19-20 (served May 25, 1999); *Conrail*, slip op. at 47.

profit-maximize at the same time The translation of these sorts of savings to real competitive benefits to shippers is long-recognized. As the Board has observed, the "clear trend" since the passage of the Staggers Act is that "when railroads have reduced their costs through mergers or otherwise, those savings have largely been passed on to their shippers in terms of lower rates and improved service."[18] The Board's treatment of cost reductions and related efficiency gains finds support among its sister agencies, in particular the DOJ, FTC, and FERC. The DOJ/FTC *Merger Guidelines* observe that:

> mergers have the potential to generate significant efficiencies by permitting a better utilization of existing assets, enabling the combined firm to achieve lower costs in producing a given quantity and quality than either firm could have achieved without the proposed transaction. Indeed, the primary benefit of mergers to the economy is their potential to generate such efficiencies.[19]

The *Guidelines* then take the next important step, recognizing that such cost savings efficiencies "can enhance the merged firm's ability and incentive to compete, which may result in lower prices, improved quality, enhanced service, or new

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18 *Union Pac. Corp.—Control and Merger—Southern Pac. Rail Corp.*, 1 S.T.B. 233, 370 (1996), *aff'd sub nom. Western Coal Traffic League v. STB*, 169 F.3d 775 (DC Cir. 1999); *see also CN/IC*, slip op. at 20 ("efficiency gains, in varying degrees depending on competitive conditions, have generally been passed on to most shippers as reduced rates and/or improved services"); *Conrail*, slip op. at 47 (same).

products."[20] The Board's n precedents and the views of fellow regulators thus strongly suggest that merger-related cost savings efficiencies can be important competitive enhancements. Thus, even if cost savings might be less than in past mergers among competing railroads, the Board still ought to count them along with new competitive offerings when weighing the potential competitive benefits of a transaction against its potential competitive harms.

B. The Proposed Rules Should Be Modified or Clarified to the Extent that They Could Require Benefits to Competitors that Do Not Address Merger-Specific Harms

The Board observed in its commentary to Proposed § 1180.1(c), that competitive enhancements "need not be directed at remedying specific competitive or other harms that are threatened by the merger. As discussed above, the "competitive enhancements" given as examples envisioned in the proposed rule may not in fact enhance competition at all, and could even hinder economically efficient alternatives extant in the marketplace or created by the transaction. Even assuming, however, that these "enhancements" would not indeed constitute a substitution of regulatory judgments for market judgments, to the extent they do not address directly competitive harms sponsored by the merger, they are

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19 U.S. Department of Justice and Federal Trade Commission, *Horizontal Merger Guidelines* § 4.0 (issued 1992 and rev. 1997), *reprinted* 4 Trade Reg. Rep. (CCH) ¶ 13,104.

unwarranted and likely would lead to perverse results; results themselves contrary to the public interest.

1. The Board's Language Leads to the Destruction of the "Existing Conditions" Doctrine with Potentially Disastrous Procedural and Practical Consequences

A well-established principle of the Board is that merger conditions are imposed to cure only transaction-related problems, not existing situations. Under this existing structure, commenting parties appropriately are discouraged from treating rail combination cases as an occasion to seek conditions to remediate existing situations. The Board repeatedly has explained that it "will not impose conditions 'to ameliorate longstanding problems which were not created by the merger,' nor will we impose conditions that 'are in no way related either directly or indirectly to the involved merger.' "[21]

As a corollary to this, in the past, the Board has not taken the view that problems caused by a transaction — or for that matter putative inherent vices in a transaction — could be cured, if cure were necessary, otherwise than by cures addressing the problem in question. It was on this basis that CSX believed in its

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20 *Id.*

21 *UP/SP*, slip op. at 145 (citations omitted); *see also BN/SF*, slip op. at 56 (citations omitted). The Board's predecessor found that "requiring a merged carrier

filings responsive to the ANPR that the problems of implementation difficulties should be dealt with by requiring an implementation plan, including capacity plans both for fixed infrastructure and for rolling stock — a recommendation with which the Board seems to be in solid agreement, at least in principle.

Under this (the existing) structure, the Board was in a position to warn parties making comments or seeking conditions, as it and its predecessor historically have done, that rail combination cases are not to be viewed as an occasion for remediating existing problems.[22] Thus, for example, in the Conrail transaction, shippers that were served by a single rail carrier and not made part of a shared assets area were denied, properly, their claims to the Board that if others had the direct benefits of a shared assets area, it was right and proper that they have them themselves. The same was the case with carriers who complained of perceived dispatching problems, or shortlines who complained that their existing

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to protect carriers against circumstances which were not caused by the merged carrier does not appear fair." *BN/Frisco*, 360 I.C.C. at 952.

22 If the transaction was perceived as causing a problem in any specific locality that did not exist before, the applicants knew that the Board might require specific remediation and so would attempt to provide it in their application. If the Board viewed the remediation as inadequate, it might impose some conditions aimed at specific remediation of problems caused by the transaction; if the problem was major and remediation was impossible or destroyed the benefits of the transaction, the application would be denied.

interchange rights were limited. Preexisting conditions such as those — however vexing to the complainant, however sympathetic the complaint, and however beneficial to some party or another the requested "fix" might be — simply had no nexus to the transaction and were not the proper subject for dispute in a rail combination case.

The Board's doctrine allowed requests for the correction of preexisting situations to be summarily denied, without placing the Board in the highly difficult situation of weighing the good that would be done to a shipper or shortline in one state against the good that would be done to a shipper or shortline in another state if only one or the other's existing problem were solved by the Board's conditioning power. (We assume that the Board is not suggesting that the transaction must cure <u>all</u> existing shipper problems in order to provide a net benefit to the public interest.)

The language used by the Board appears to do away with this established method of examination and adjudication. The language seems to say that possible congestion that might occur in Pennsylvania can be expiated by the Board's requiring an increase in the number of rail carriers serving particular shippers in Duluth, MN; or that a reduction of intramodal competition in Kansas might be counterbalanced by the Board's reducing switching charges in Oregon, even though the transaction otherwise has no effect whatsoever on Oregon.

If that is the Board's intent, the consequences, we suggest, should make the Board examine — and reexamine — the point very carefully. Such an interpretation and approach would sound the death knell of the "preexisting problems" doctrine under which a very substantial percentage of the pleas for relief requested by commenters and other condition-seekers in a rail combination proceeding are disposed of.[23] That theory, which demanded a relationship of cause and effect involving the transaction, logically could no longer survive. Even through the transaction has no effect on Oregon, and even if the likelihood of congestion in Oregon is relatively slight, there is likely to be some congestion in some other locations as a result of the transaction, despite best efforts to avoid it. This now seems to be the "original sin" of rail combinations which, under what the Board sometimes seems to be saying, must be counterbalanced by some action perceived by the Board as beneficial to some interested parties. If that is really the

[23] In one of its most recent reviews of an end-to-end merger, the Board rejected shipper requests to force interswitching on the applicants CN and IC to all major connecting railroads. The Board said that such a forced access condition "would result in a fundamental restructuring of applicants' relationships with connecting carriers" without any showing of a nexus between the relief sought and the merger.

case, why rule out a reduction in switching charges in Oregon as a counterbalance to congestion in Kansas? Since a connection between the harm and benefit is no longer to be demanded, and since presumably whatever the applicants propose as to their set of competitive enhancements is not going to be simply rubberstamped by the Board, a plea by a shipper group in Oregon for a reduction of switching rates would be as much worthy of consideration as any other proposal made either by the applicants or by the dozens of interests which now appear in rail combination cases, whose number would only be increased by this change. It is a rare shipper or shortline that does not have some perceived problem that it could ask the Board to "cure" if economic cost were of no concern.

The Board thus would be placed in the impossible position of picking "winners" and "losers" in a process that has little to do with the merger itself. Prioritization among the requests — to be determined free of connection to any transaction harm — would have to be effected. There would be no guidelines for this, because the existing guidelines are that preexisting situations would not be dealt with at all.

STB Finance Docket No. 33566, Canadian National R. Co.—Control—Illinois Central Corp. *et al.* at 39.

The adverse effect this would have on the economics of the proposed transaction, and its other offenses against sound principles of regulation, are discussed in the remaining subparts of this section. Its effect on the Board's processes, and on the already daunting period of time it takes for those proposing a rail combination to obtain the Board's judgment on it, must be considered. The Board's last transaction involving two or more very large rail carriers, the CSX/NS-Conrail transaction, took a period of 13 months from application to authorization; preparation of the application took close to three additional months. While the transaction had certain unique aspects (the split of an existing large carrier between two other large carriers), the death of the "preexisting problems" doctrine is apt to make up for (if indeed it will not more than make up) any savings in processing time that a less complex transaction might involve.

The result of this change would mean a larger, busier, more populous, more complex proceeding even than has previously been encountered. Instead of improvement in processing time so that it would even closely resemble that which the rest of American industry experiences in a merger outside of a regulated industry, there would be an inevitable increase in processing time until it filled the outside limits of the statutory period is set forth in 49 U.S.C. § 11325. Indeed, the proposed rules seem to contemplate this; proposed §1180.4(e) describes no more expeditious goal than that of the statutory maximum.[24]

The ill effects of abandoning the "existing situation" rule and cutting the nexus between potential harm caused by the transaction and remediation would go beyond the Board's own processes. The absence of established litigation-tested standards would be felt immediately in the area of judicial review. If the Board ordered any "free-standing" benefits (those unrelated to specific merger harms), parties that were not the beneficiary of the Board-ordered freestanding benefits would take the position that they were equally entitled to them as were others who received them. They would complain if the Board did not afford a comprehensive, rational explanation of why each party claiming a benefit that was not granted was so treated while others claiming and receiving benefits, also unconnected with transaction-related harm, received them. The Board would not have a basis of distinction based on long-standing practice, which the Board had in the Conrail case where at least one party demanded such an explanation, to use in responding to such an assertion. The long-settled practice of not dealing with existing situations would by definition have been formally abandoned. The likelihood of possible stays of the Board's decision, bringing about further delay in the

24 We discuss this further in part D, below.

transaction, would be presented, as would the vexation of remands to the Board for a reevaluation of the basis of the respective grants and denials of transaction-unrelated benefits. The result of that can hardly be positive.

The Board should take care to make it plain that in its balancing test for a transaction, a close relationship between the principal adverse effects of transactions and the ameliorating benefits relied upon will be the Board's touchstone, and that the "preexisting problems" doctrine remains alive and well.

CSX believes that a proper evaluation of how competition can be enhanced in rail mergers and a "cause and effect" standard — dealing with implementation problems by trying to avoid them and directly remediating and untangling them; dealing with specific competitive problems caused by the transaction by remediating them, *etc.* — would fulfill the positive goals that the Board has established in its NPR. That approach would maintain the "preexisting problem" principle and would avoid the procedural and forensic morass that abandoning that principle would create.

2. Use of Merger Conditions to Reregulate the Industry Is Outside the Board's Conditioning Authority and Inappropriate as a Matter of the Statute and of Policy

The Board has observed that its conditioning powers, however broad, do not empower it to alter market-framed ownership interests that are not implicated by a proposed merger. As the Board observed in its commentary to Proposed § 1180.1(d), "we do not believe that it is appropriate for us in the first instance to attempt to use our broad conditioning powers to impose through merger approvals a broad program of open access that would go beyond the public interest balancing in our proposed merger policy statement and would otherwise be contrary to our statute and the policies it embodies." (Emphasis added.)

When conditions address a potential harm sponsored by the merger, they properly find their source in the authority Congress gave the Board to condition mergers. If the competitive "fix" bears no relation to the likely harm identified, however, then the fix would constitute nothing less than the use of conditioning powers "in the first instance" rather than as a tool to address and correct a problem with the merger. The proposed rule could be read to suggest that the Board intends to do just that. The rule would presume anticompetitive harm and effectively require that applicants proffer fixes to weigh against the presumed anticompetitive effects, and it solicits fixes unrelated to an identified threatened harm.

Congress gave the Board the power to condition mergers it approves "to alleviate anticompetitive effects of the transaction . . . ." 49 U.S.C. § 11324(c). As developed in part 1 of this Section, if an anticompetitive effect is foreseen in Chicago, it is not going to be alleviated by a grant of trackage rights in California or New Mexico. Requiring such forced access either to counterbalance a presumption of harm or an identified but unrelated post-merger harm does not address any identifiable harm and alters existing ownership rights in ways that the Board otherwise would have no authority to do. Although the Board recognizes that a broad-based program of such forced access unrelated to merger harms is beyond its authority,[25] the proposed rules would depart in a significant way from this important principle by treating favorably a piecemeal approach to the same end.

Moreover, because under the proposal a "fix" need not address the problems presented by the merger, it will be difficult to quantify the degree of fix in one market necessary to counter-balance the degree of harm in another. This is why other competition authorities address the likely harm from an acquisition by determining whether the fix preserves the degree of competition in the identified market premerger.[26] Under the established approach, by focusing the fix on the likely harm, competition authorities evaluate apple against apple, and avoid problems of overkill or under-protection that could flow from policies aimed at

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25 *See* NPR, at 16-17.

26 *See, e.g.*, *United States v. Republic Svcs., Inc.*, 65 Fed. Reg. 54,547 (Sept. 8, 2000) (consent judgment remedying only merger-related harm in relevant market); *United States v. SBC Communications, Inc.*, 65 Fed. Reg. 56,926 (Sept. 20, 2000) (same); *In re Novartis AG*, FTC Docket No. C-3979 (Nov. 1, 2000) (same); *In re*

broader reregulation of the market's forces. Thus, the procedural and evaluative problems highlighted in part 1 meld with the substantive difficulties inherent in the Board's language. Of course, the overall procompetitive efficiencies and other benefits of a merger can overwhelm minor competitive concerns, but fixes designed to create the appearance of efficiencies are themselves problematically inefficient.

3. Requiring "Enhancements to Competition" that Are Unrelated to the Merger Is Inconsistent with the Board's Requirement that Benefits Be "Merger-Specific"

In Proposed § 1180.1(c), the Board makes clear that, in evaluating the public interest, it considers whether the benefits claimed could be realized by less restrictive means than a consolidation, pointing to joint marketing arrangements and interline partnerships as examples. Indeed, such arrangements can promote efficiencies without a change in control or complete melding of finances, and where a Class I merger's efficiencies are not larger than those that could be achieved by less restrictive means, the Board intends not to credit those benefits to a proposed merger. In that sense, it is correct to say that benefits must be "merger-

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Agrium, Inc., FTC File No. 001-0100 (Aug. 10, 2000) (same); *In re Boeing Co.*, FTC File No. 001-0092 (Sept. 27, 2000) (same).

specific."[27] The proposed rule, however, appears to diverge from the same correct principle where, in the commentary to the very same section, it is stated that "new competition need not be directed at remedying specific competitive or other harms that are threatened by the merger." *See* NPR at 13.

Just as benefits should be merger-specific, so should conditions designed to address harms. The policy basis for consistency here is more than an objective desire to promote symmetry. By requiring the benefits to be merger-specific, the Board is focusing on whether the merger causes the benefits. Unwilling to credit benefits that can be achieved by lesser means, the Board is weighing the competitive benefits caused by the merger against the competitive harms caused by the merger. By seeking to require a generic and potentially boundless class of unrelated "competitive enhancements" designed to tip the scales, the Board would promote changes to asset control and utilization not caused by the merger, but caused solely by the regulatory process as a "toll." As addressed above, there is every reason to believe that many of these "enhancements" do not make economic sense in the marketplace, and only would be entertained by the merging parties as a means of gaining regulatory clearance — paying the "toll."

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27 This is the same basic standard employed under Section 4 of the DOJ/FTC *Merger Guidelines*.

The absence of any connection of these "enhancements" with the competitive or other potential harms, moreover, makes weighing them difficult. Applicants will be forced by the Board's language to make such guesses, increasing the uncertainty associated with the process and promoting claims of arbitrariness by shippers and other railroads not directly affected by "enhancement." Keeping the analysis on a "merger-specific" level will avoid this outcome.

4. Requiring "Competitive Enhancements" Unrelated to Merger-Caused Harms Will Discourage Creation of Future Shortlines and Will Harm Shippers

An example given by the Board in its list of possible competitive enhancements is the lifting of so-called "paper barriers." Most shortlines came into being through rail spin-offs that addressed specific issues of service to customers, often in competition with trucks. The agreements negotiated for those spin-offs provided rights to the new entrants designed to ensure their viability under proper management and acceptable to the entrepreneurs who executed them and assumed leadership of the new companies. The agreements did not contemplate wealth-redistribution or reregulation of the industry.

Requiring "competitive enhancements" to undo these freely negotiated limitations where they do not relate to any likely competitive harm not only unfairly penalizes railroads which effected spin-offs *ex post facto*, but it would discourage future spin-offs as well. Removing the contractual provisions will also have an adverse impact on the economics of rail networks, dilute revenues realized by Class I railroads, and ultimately affect decisions on how to deal with branch lines — all potentially likely to affect shippers adversely. Rather than undoing contracts as a sort of merger tax, the Board, as it did in the Conrail case, should ensure that contractual restrictions are not expanded by consolidations.

5. Broadening Access Rights by Other Railroads Will Adversely Affect the Consolidated System's Network and Complicate Integration Planning

The sweeping imposition of access conditions not limited to those necessary to remediate identified competitive concerns will significantly adversely affect the achievement of the consolidated system's network. Moreover, at the very time when merger integration planning is most challenging, and at a time when the planning process will receive the most commentary and review, making it more difficult, a proposal for "enhanced competition" that introduces new operations by others in various locations of the rail network will further complicate the process. Ordering such operations and changing the flow, density and other key operational considerations, will not benefit shippers but rather will harm them. This is unlike the grant of access to alleviate a specific competitive harm. We must not forget the difficulties that have accompanied the two largest most recent mergers, and it would be irresponsible to burden the planning process and, more vitally, the reallife integration itself with additional operators on the properties providing a general "enhancement" to competition unrelated to merger harm. In the instant case, when the fix is unrelated to the potential harm, there is no such relationship, and because of the network effects of such changes, will likely complicate the process of integration. The forced introduction of operations by others and the disruptions that it can cause ought only to be a remedy for a specific competitive problem.

C. The Rules Properly Require Service Assurance Planning Which Is Most Effectively Done Through a Flexible Iterative Process

There are two fundamental aspects of service assurance that the Board's proposed rules support. First, the Board places the onus on the applicants to develop service assurance plans, while itself undertaking the responsibility for operational monitoring during the oversight period. Thus, the Board wisely has avoided substituting regulatory judgments for those of responsible rail managers. Second, the Board properly rejected proposals that it be turned into a claims tribunal, and instead has left such matters to well-established modes of dispute resolution.

By requiring applicants to address the integration of operations, coordination of passenger operations, yard and terminal activities, infrastructure improvements, information technology systems, customer service, labor, training, contingency plans and timetables, the Board gives all interested parties the opportunity to provide the Board (and the applicants) with the kind of meaningful input needed to ensure an efficient process. Furthermore, by focusing the operations integration information on route-level movements rather than shipper-by-shipper movements (§ 1180.10(a)), the Board strikes the pr 'ance that allows shippers to address concerns while keeping the focus . particularized debates but on the needs of broader groups of the shipping

The Board's proposed rules should adopt a flexible and iterative process, as proposed by CSX in response to the ANPR. Transition planning, like any form of learning or applied learning, is a management process, not simply a regulatory report, and the best transitions will evolve considerably. Doubtless, all of the U.S. Class I railroads have learned much from past integration problems, and each that may be involved in a merger likely will initiate processes and safeguards to guard against the types of problems encountered in the past and which past experience counsels to guard against in the future. Still, identifying and prognosticating all of the effects that integration will have on service in advance of the integration is not enough. As an integration plan unfolds, market and other conditions change. This means not only that other Class I, II and III rail carriers can be expected to react

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28 Doing so may remove the risk of balkanizing merger conditions that eat away at the overall efficiency of a route, or the entire network, that benefits all shippers.

competitively to the applicants' operating plan, but so do trucking companies and other intermodal elements. Predicting and quantifying all of these in advance so that they are fully anticipated during the Board's years of oversight is not realistic. Such a "snapshot" approach to an evolving situation invites protracted debate over the causes behind shifting market conditions.[29]

The critical importance of permitting the Applicants to adjust their plans as the integration unfolds is illustrated by just a few examples of CSX's recent experience in integrating the Conrail lines into its system:

The Application's traffic studies, which were based upon accepted methodologies that predict transaction-related traffic diversions, indicated that in the important St. Louis to East Coast corridor, over 500 cars per day would be diverted by Norfolk Southern away from the Conrail (now CSX) route via Avon Yard in Indianapolis. CSX's planners took advantage of this forecasted added capacity at Avon Yard and designed the operating plan to shift St. Louis-to-

29 Shifting costs borne differently by different transportation modes and companies can have serious effects on the cost of service, and therefore, the competitiveness of relative service offerings. In December 1999, when crude oil was trading at $8 a barrel, it would have been prescient indeed to predict it would be at $35 a barrel within about six months. Nonetheless, fluctuations in input prices like these make it quite difficult to predict how competitive a force a competitor will be, especially as an integration progresses.

Cincinnati traffic into Avon. This would focus more east-west traffic into a single hub. But as it turned out, CSX's aggressive competition in the pre-Split commercial negotiations with shippers caused most of that traffic to come to CSX. Avon Yard was flooded with cars. Adjustments to the operating plan had to be made to run through and/or bypass the yard.[30]

Again, competition by CSX for traffic to and from the North and South New Jersey Shared Assets Areas put tremendous stress on the River Line between the greater New York/New Jersey area and Albany. This single-track line would have been sufficient for the traffic CSX predicted, but could not accommodate the volume it was required to handle. CSX reacted by adjusting the operating plan, moving some trains southward via Baltimore/Philadelphia and by adding unplanned sidings to the River Line as soon as possible.

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30 And, with or without the right guess about the marketplace, there are plans that simply do not work out. CSX intended to operate its Willard, OH yard as a "block swapping" yard, with trains scheduled tightly to arrive carrying specific, planned blocks. These blocks would then be quickly combined into outbound trains. The plan was well conceived and would have operated efficiently if the required reliability in arrival times could have been accomplished. In the event, however, it proved simply too difficult to perform. The need to meet schedules so rigorously made the plan inflexible and vulnerable to even routine train delays. Accordingly, CSX planners totally changed the role of Willard Yard, converting it to a westbound classification role, and transferring the eastbound classification role to Cumberland Yard. This was done in an intensive effort over a single weekend, with implementation accomplished in days.

In each of these instances, CSX was free to make the much-needed changes to its operating plan without regulatory process. No petition for modification had to be submitted; no formal approval had to be sought. Instead, the Board's Operational Monitoring team was kept fully advised, first of the difficulties that were being encountered, then of the changes planned, and finally on the success of the changes to the plan. Furthermore, shippers were kept abreast of these changes through the Transaction Council, permitting them to plan and adjust to changes. The public interest was protected by ensuring that the railroaders responsible for running the railroad had the freedom to solve the problem, unencumbered by a regulatory process, while the authorities responsible for monitoring were kept fully informed at all times.

Not all merger benefits, including efficiencies, can be predicted fully at the outset, and efficiencies that lower cost of service will benefit shippers as the merged carriers find it profit-maximizing to lower prices. As these benefits present themselves, the applicants may well be faced with the choice of modifying the plans outlined in their service assurance plan and risking dissatisfaction of a small element of shippers or making changes that would benefit a larger number of shippers. A snapshot approach coupled with an overview process of a nature that would tend to freeze planning will undermine the realization of these newly discovered procompetitive benefits. If realizing such procompetitive benefits results in a net positive, but has some associated cost, the cost might be treated as an inability to meet the service assurance plan. Despite the fact that the change could benefit many more shippers than it hurts, if the system is unduly rigid, applicants likely would be reluctant to act from the prospect that the oversight rules might impose penalties on such procompetitive choices. Such a reluctance should not be encouraged. Real-world history shows that mid-course corrections in plans often benefit many shippers while doing little or no harm to others.

For example, the CSX Operating Plan anticipated extensive rehabilitation of the Ft. Wayne Line (roughly, between Ft. Wayne, IN and Chicago) to provide an alternative to the B&O main line to Chicago. The B&O line was double tracked in one of the largest rail capacity-expansion projects in recent decades, but the Ft. Wayne Line has not been rehabilitated as yet.[31] The postponement of the Ft. Wayne line work has become prudent for several reasons. First, the B&O line — particularly with the revisions to the operating plan — has proven itself capable of handling the day-to-day traffic demands placed on it. Second, the pressing need for expansion of capacity on the River Line dwarfed the benefits of adding an

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31 While the Operating Plan, of course, projects operations on a given assumed traffic base at the end of three years, the Board's rules do not mandate that all changes contemplated be made within that time.

alternative route to Chicago. Third, capital constraints have made it increasingly difficult to invest in infrastructure and the Ft. Wayne line project must compete for scarce capital dollars with other desirable projects such as expansion of capacity in the heavily used Philadelphia-to-Baltimore corridor. Clearly, shippers have gained more from the expansion of the River Line's capacity than they would have realized from rehabilitation of the Ft. Wayne line.

It is significant that the Board has not historically imposed the terms of an applicant's operating plan as a condition, nor otherwise required slavish adherence to it. Because of that policy, CSX was able to make the necessary changes to its operations and infrastructure projects to work through the service difficulties in encountered in the integration on a real-time basis. That is, CSX was (and is) able to react, adjust and improve without seeking permission from the Board and without having to debate its managerial decisions in a forensic encounter with third parties who might prove willing to litigate every change — either to pursue benefits to themselves, or to seek leverage in negotiation of unrelated issues with the carrier.

Another advantage of allowing a more iterative process is that applicants more easily can accommodate the ongoing comments of third parties, formal or informal. With the snapshot approach, following through on comments may create ripple effects in the rail network that could result in charges that service assurance is not being met, although the overall effect is beneficial.

Finally, a more iterative process will in no way limit the Board's ability to review the representations made in the application through its oversight process because the Board will be able to track the development of the integration process as it is articulated to its staff. In fact, because the process would be designed to lay out the initial plan first, and then iterations of it based on choices made in response to third-party comments, market conditions, and other factors that influence railroad choices in a competitive world, there will be more of a roadmap made available to the Board's oversight process than contemplated by the proposed procedure.

D. The Period for the Board's Review of Proposed Acquisitions Should Be Shortened

Inasmuch as the Board's proposed rules increase the uncertainties associated with regulatory review of Class I rail mergers, the process would better serve all interested parties if it were shortened. By making use of presumptions of anticompetitive effects, service integration failures and the like, and requiring counterbalancing "competitive enhancements," which require an apples versus oranges weighing of public benefit factors, the Board's proposed rules heighten the uncertainty of outcome of applications for rail mergers and grossly protract the process of review, as discussed in part B., above. Furthermore, by requiring more up-front planning than ever before, coupled with "at least" five years of oversight, the Board's proposed rules promise that the information necessary to do this job of reviewing the transaction is at hand, and the means to address developments that somehow escape the process lie in reserve.

There are a number of benefits that would be derived from a shorter review period. First, there is need for direction and closure in operating any business, particularly a transportation network. Second, integration planning is better if it is not dragged out, so that changing market conditions over time can affect it as little as possible.

1. The Need for Closure

The goal of seeking closure and certainty is not inconsistent with the worthy goals of ensuring that interested parties be heard and that the Board carefully evaluate a transaction. Closure benefits not only the applicants, but shippers, labor and other railroads. Seeking closure should be one of the goals behind these proposed rules, and they should be fashioned to facilitate certainty consistent with achieving overall public benefit.

A merger review process is costly in many ways, particularly to the seller:

- Skilled employee attention is diverted to the drafting and prosecution of the application;
- The applicants lose employees who self-select to find positions elsewhere;
- Shippers can view the uncertainty of the process negatively and choose other shipping options, both rail and other modes;
- Efficiencies and other benefits are not realized as quickly, the longer the process is dragged out.

If the final rule has the effect of introducing more difficulty to the merger process through additional plans, more commentary, broadened issues, abandonment of the "existing problem" rule, or otherwise, it will raise the level of uncertainty associated with the process. This will accentuate the costs listed above. Because those costs fall inordinately on the shoulders of the applicants, during the pendency of the review, one or both of the applicants could become a less effective competitor, affecting shippers, among others. More importantly, if the process results in a denial of the application, it is even more important that the process be swift. That way, the carriers involved have a better chance of regaining their competitive footing or, better yet, not losing it in the first place.[32]

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32 Additionally, as integration inefficiencies rise, shippers' perceived costs of dealing with applicant carriers increase, causing them to substitute away from the

2. The Impact on Integration Planning

The marketplace and competitors will not stand by while the Board reviews a merger application. The Board's proposed rules would promote uncertainty by making merger approval more lengthy and complex. This, in turn, will make even more difficult the efficient integration of merging carriers. Such a result is particularly inappropriate given that any future merger likely will be end-to-end, will involve very few competitive overlaps, and thus fewer significant competitive issues. The major issues such a proposed merger is likely to raise will focus on the ability of the carriers to accomplish an expeditious and efficient integration. The process itself ought not be one of the significant impediments to successful integration. Moreover, the delay and cost of the process works as a tax on the benefit of the merger, and an impediment to efficient mergers.

For all of the above reasons, it is more important that greater emphasis be placed on integration planning and that the process be shortened.

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merging rail carriers. This is an inefficient result brought on by the review process that also is unnecessarily costly to the merging carriers.

E. The Proposed Labor Provisions Properly Favor Negotiated Terms, but They Should Not Go Beyond Past Precedents to Create Such Agreements

The Board is proposing to amend the existing rule concerning labor protection, Section 1180.1(f), to reflect "our continued emphasis on negotiation, without direct Board involvement, between the unions and railroad management to resolve merger implementation issues." NPR at 17. CSX is also supportive of early consultation and negotiation as the preferred method for reaching implementing agreements required by the Board's employee protective conditions. The overwhelming majority of the numerous ICC or STB approved transactions that CSX or its predecessors have implemented over the years have been accomplished pursuant to implementing agreements, which were the product of voluntary negotiation. For example, in the recent Conrail transaction, implementing agreements were reached with all of the unions, except one, through negotiation. Even in this one case, after arbitration, the parties subsequently reached a voluntary implementing agreement.[33]

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[33] Two other arbitrations were necessary to resolve limited intra-union issues in otherwise negotiated agreements. A fourth arbitration was necessary to impose the negotiated implementing agreement which was not ratified by one of the involved Unions. *See also* First Submission By Applicants CSX Corp. and CSX Transportation, Inc., STB Finance Docket No. 33388 (Sub-No. 91, at 32-33 (June 1, 2000).

Furthermore, CSX, along with other major railroads, through the National Railway Labor Conference ("NRLC"), has negotiated an agreement with the United Transportation Union ("UTU") concerning the future utilization of the Board's authority to modify collective bargaining agreements in major transactions. In other transactions, the Board's existing standards would continue to govern. CSX and the other major railroads are also attempting to negotiate similar agreements with the remaining rail unions. The other unions, unfortunately, have suspended their participation. CSX believes that these negotiations should be restarted and that a consensus can be reached based upon the UTU-NRLC agreement.

CSX, however, does not see any basis for the proposed amendment of the Board's regulation to add the following language in new Proposed Section 1180.1(e): "[T]he Board respects the sanctity of collective bargaining agreements and will look with extreme disfavor on overrides of collective bargaining agreements except to the very limited extent necessary to carry out an approved transaction." Sometimes negotiations do not produce an agreement. In those circumstances, the Board's arbitration procedure and Board review are available to ensure that labor disputes do not frustrate an approved transaction which will benefit the public. Indeed, 49 U.S.C. § 11321(a), as interpreted by the

Supreme Court, mandates that collective bargaining agreements be modified when necessary to allow implementation of an approved transaction.

The Board, and before it the ICC, have consistently recognized for over 20 years that modification of collective bargaining agreements is necessary in virtually every railroad consolidation. For example, in *Carmen III*, the Board quoted with approval the observation in *Carmen II* that "in many instances, preservation of the CBA status quo would effectively thwart full implementation of rail carrier transactions. . . ."[34] The Supreme Court and D.C. Circuit similarly have recognized that modification of collective bargaining agreements is almost always necessary to realize the efficiency of approved transactions.[35] Rail operations, facilities, and employees simply cannot be combined unless the scope, seniority, and other collective bargaining agreement provisions are modified. The inability

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34 *CSX Corp. - Control - Chessie System, Inc. and Seaboard Coast Line Industries, Inc. (Arbitration Review)*, Finance Docket No. 28905 (Sub-No. 22) (served Sept. 25, 1998), 1998 STB LEXIS 497, *36. *See also, e.g., CSX Corp. - Control - Chessie System, Inc. and Seaboard Coast Line Industries, Inc.*, Finance Docket No. 28905 (Sub-No. 22), 1990 ICC LEXIS 222, 13 ("inevitable conflicts with CBAs. . . .").

35 For example, the D.C. Circuit stated that the need to modify collective bargaining agreements was "both obvious on its face and was demonstrated by CSXT." *United Transportation Union v. STB*, 108 F.3d 1425, 1431 (D.C. Cir. 1997). *See also, e.g., Norfolk & W. Ry. Co. v. Am. Train Dispatchers Ass'n*, 499 U.S. 117, 133 (1991) ("rail carrier consolidations would be difficult, if not impossible, to achieve.").

to reach a voluntary agreement cannot be allowed to thwart the implementation of a transaction, which has been found to be in the public interest.

The UTU-NRLC agreement in fact recognizes that some collective bargaining agreement modifications are necessary. While there may be a controversy over the extent of the required modification or the selection of a single collective bargaining agreement, it has never been accepted that some contract modifications would not be necessary.

For these reasons, there is no basis for the Board now to "strongly disfavor" collective bargaining agreement modifications. The proposed statement will encourage unions to oppose even necessary collective bargaining agreement modifications, thus making it less likely, rather than more, that voluntary implementing agreements will be reached. In its *Carmen II* and *Carmen III* decisions, the Board has already removed any basis for a perception that the *New York Dock* procedures favor carriers over labor. And, of course, Board review of arbitrated outcomes is available.

The Board is also encouraging railroads and rail labor to reach an agreement that would resolve other issues relating to its labor protective conditions. The Board's explanatory note states that "we have proposals before us, which we are seriously considering, for new rules to govern contentious issues, such as the need for employees to relocate in order to retain their jobs."

The relocation issue is currently again before the Board in *Norfolk Southern Corp. -- Control -- Norfolk & W. Ry. Co. and Southern Ry. Co. (Arbitration Review)*, STB Finance Docket No. 29430 (Sub-No. 21) (served Dec. 15, 1999). This and other proposals for modifying the Board's employee protective requirements should be evaluated on their own merits. However, CSX would note, though, that it is not unusual for employees to have to relocate as a result of mergers and consolidations or to voluntarily relocate through the exercise of their seniority. This is commonplace in the railroad and other industries and in government. Allowing railroad employees to refuse to relocate, when jobs are available, would adversely affect the railroad's ability to provide service and impose unnecessary costs. The railroad would lose valuable, experienced employees. And, at the same time the railroad is paying those employees protection, it would have to hire, train, and pay new employees to fill the positions, which the experienced employees refused. This would be a "lose, lose situation." The Board recently refused a request by rail labor to waive the relocation requirement in its approval of the Conrail transaction. The Board recognized that "a basic part of the bargain embodied in the Washington Job Protection Agreement upon which the New York Dock conditions are based" is that rail carriers are permitted to relocate employees in order to "achieve the benefits of a merger transaction in return for up to 6 years of income protection and various other benefits."[36]

In conclusion on this point, CSX suggests that the Board modify Proposed Section 1180.1(e) by deleting the sentence "Otherwise, the Board respects the sanctity of collective bargaining agreements and will look with extreme disfavor on overrides of collective bargaining agreements, except to the very limited extent necessary to carry out an improved transaction." Further, CSX suggests that, with respect to the relocation issue, no change in the current labor protection conditions is warranted.

F. The Operation of the Board's Voting Trust Rules Is Not Broken and Accordingly Should Not Be Fixed

Proposed § 1180.4(b)(4)(iv) introduces a new requirement into the use of voting trusts in transactions involving two or more Class I rail carriers. CSX believes that the revision is not needed, unfairly disadvantages rail combination transactions in the marketplace, would increase litigation, and would place the

36 *CSX Corp. and CSX Transp., Inc., Norfolk Southern Corp. and Norfolk Southern Ry. Co. -- Control and Operating Leases/Agreements -- Conrail Inc. and Consolidated Rail Corp.*, Decision No. 89, STB Finance Docket No. 33388 at 128 (served July 23, 1998).

Board in the awkward position of making "public interest" determinations on the basis essentially of the names of the parties involved in a proposed transaction.

Today's corporate merger and acquisition techniques operate rapidly through tender offers made with deadlines of generally 20 business days[37] (approximately a calendar month) or with stockholder votes taken within a few months of the announcement of a transaction. These rapid timetables are grossly inconsistent with the Board's usual processing times in major merger transactions, and indeed, even with expedited timetables, such as 180- or 270-day periods between the filing and closing of the evidentiary record. Indeed, these marketplace techniques regularly involve time schedules that are shorter than the three-month waiting period required between filing a Notice of Intent and filing the Application with the Board. In response to these facts, and to put as far as possible regulated railroad merger and acquisition transactions on a level playing field with other market transactions (including unregulated acquisitions of rail carriers), the Board has promulgated Part 1013 of its rules, 49 C.F.R. § 1013.1 *et seq.* That part provides standards for an independent voting trust into which the stock of one of the rail carriers or entities controlling a rail carrier may be deposited, so the financial aspects of the transaction may be effected (subject to divestiture) in advance of the Board's careful determination of the "public interest" requirements necessary for approval of a major transaction within its jurisdiction.

Divestiture of the stock in question by the voting trustee is required if the transaction is not approved by the Board. Certain requirements for the voting trust instrument, for the independence of the trustee, and for the irrevocability of the trust, are set forth in rule §§ 1013.1 and 1013.2. Procedures and reporting requirements concerning voting trusts are set forth in § 1013.3.

In § 1013.3(a) an optional provision for informal review of voting trust agreements is made, under which the Board's staff will give an informal, nonbinding opinion as to whether the voting trust effectively provides insulation against unauthorized acquisition of control of the carrier whose stock (or the stock of whose holding company) is to be placed in the trust. As a matter of practice, such opinions are given by the Board's Secretary, with input from other personnel of the Board's staff. It is probably fair to say that, at least in transactions of any size, it is universal that a submission to the Board's staff is made under that provision of the rule. The submissions requesting these opinions and the opinions themselves are public documents and are available to the public in the pertinent

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37 The minimum period established by SEC Rule 14E1(a) under the Securities Exchange Act of 1934, as amended, for tender offers.

Docket. The Board's staff's requests for modifications and the form of agreements that have been the subject of informal clearances by the Board's staff are often used by practitioners as guides and models in determining the appropriate clauses to be contained in these agreements. The use of these voting trusts has been sanctioned by the courts on repeated occasions. *See Water Transport Ass'n v. ICC*, 715 F.2d 581, 583 and n.1 (D.C. Cir. 1983) (collecting and citing numerous cases); *Tu v. Santa Fe Pacific Corp.*, 141 F.3d 1179 (9th Cir. 1998) (unpublished). The voting trusts are accepted for what they purport to be, a means for using market methods for effecting railroad combinations without creating a situation of unlawful unapproved control.[38]

The acts of the Board's staff in giving these opinions are not the acts of the Board, as the opinion letters habitually, very carefully, say. A party believing that a particular voting trust does not adequately insulate the corporation whose stock is in trust from unlawful control may take the matter to the Board, following the Staff's letter, and if the Board disagrees, take that position of the Board to court.

38 Transactions before the Board and its predecessor have used voting trusts both in cases where a stockholder vote was to be taken to authorize a merger and in transactions addressed directly to stockholders, that is, tender offers, both "friendly" (approved by management) and "hostile" (not so approved).

The only issue presented, however, in such a court review (a review which appears to have been very rarely undertaken in recent years) is the effectiveness of the voting trust agreement to provide the necessary insulation. The Board is viewed by the courts as having expertise in such matters and, since practitioners follow model agreements that have received the Board's staff's prior clearance, the result is that the subject has become uncontroversial. Parties opposing such transactions rarely attack voting trusts anymore. Moreover, we believe that only one commenter raised criticisms of the voting trust procedure during the ANPR proceedings in the Spring and Summer. This all would seem to have indicated that the process was not broken, and that there was no need to fix anything.

In practice, the voting trust procedure has worked quite well and has permitted the financial aspects of regulated transactions to proceed at paces similar to those of unregulated transactions. It should be noted that what we are addressing is not simply an equalization of the financial aspects of a takeover of a major rail carrier with the takeover of a chocolate manufacturer or a brewery, but that we are also addressing the financial aspects of a transaction involving the acquisition of control over a major rail carrier by a party already controlling a rail carrier or carriers as compared to that of a takeover of a major rail carrier by a party outside of the rail industry. The latter transaction, of course, could under the Board's "single system" gloss on the statute be effected without a voting trust and indeed without any processes of the Board whatsoever. It is only fair to put those two transactions on an equal footing insofar as the financial mechanisms used to achieve them are concerned. The present rules achieve that as much as the governing statute permits.

The proposed rule would effect two changes in the present informal system: First, it replaces the informal action of the Board's staff with formal action by the Board itself. Second, it adds, as an additional standard, to the historic standard of "insulation from premature control" the broad factor of "consistency with the public interest."

The proposed transfer of the decision-making power from the Board's staff to the Board, although not the major problem with the proposed change, presents its own problems. It in and of itself (even without the change in substance) might have a compromising effect on the Board's decision-making processes as the transaction moves forward. Issues concerning control are sometimes brought forward by parties in the light of restrictive covenants contained in transaction documents, which are made available to the Board and the public only when the application itself is filed. That cannot occur until three months after the voting trust agreement is filed, together with the Notice of Intent, as the proposed rules would require. Those issues, often raised in petitions to the Board, can require the

Board to explore the interface between the restrictive covenants in the transaction documents and the provisions of the voting trust agreement.[39] While CSX would have no problem as to the Board's impartiality to rethink a decision on the basis of subsequently available documents, any earlier involvement of the Board in the review of the voting trust agreement seems to create a basis for challengers to suggest prejudgment by the Board. There seems to be no reason for the Board to be involved at the Voting Trust review stage if the only issue is the abstract effectiveness of a particular form of document in providing insulation from unlawful control, which is all that the informal advice rendered by the Board's staff involves.

Much more troublesome is the second proposed innovation, that the Board's action is to include a review of the consistency of the voting trust arrangements with the public interest. That, of course, is a judgment that, if it were to be made, appropriately could be made only by the Board itself. It, however, involves the Board in a determination which is entirely too broad and, even if narrowed, cannot be made in the absence of an Application. We are not told what the content of the

39 *See, e.g.*, ARU-6 Petition, filed July 18, 1997, in CSX/NS/CR, Finance Docket No. 33388.

"public interest" is to be in this regard. Clearly it can have nothing to do with the merits of the transaction, since all that will be before the Board at this time will be the Notice of Intent, a very short filing identifying the parties to the proposed transaction and the bare-bones form the transaction will take, a proposed timetable, a stereotyped form of protective order, the proposed voting trust agreement itself, and an assertion by the proposed applicants as to why the voting trust is consistent with the public interest. Much additional information and evidence — much more than previously required — will come later, but only at least three months later, in the Application.

Parties opposed to the transaction, for their own self-interest — who may be parties not even involved in the transportation industry as participants or customers — may attempt to broaden the issues to as to include in the definition of "public interest" the ultimate consistency of the transaction with the public interest. Their argument would be that if at the end of the line the Board is likely to turn down the transaction, would not the process of sterilizing the target carrier in a voting trust and then going through the laborious process of divestiture best be avoided by rejecting the voting trust? Such an argument would resemble arguments that are made in courts every day concerning the grant or denial of preliminary injunctions; but they characteristically involve private orderings, not determinations of "consistency with the public interest" by an agency of the

Federal Government. The Board may restrict the factors constituting the "public interest" that it will consider in passing on the voting trust, but all the evidence it will have from the applicants will be a few sketchy pieces of paper; including the Applicant's contention of what the public interest is and how the voting trust in question meets it.[40] Those materials would be enough to conclude that the form of the voting trust agreement provided on its face insulation from unlawful control, but hardly enough for the Board to make a "public interest" determination, even a narrow one. The party making the attack could be a shipper or a port with legitimate although private concerns, or it could be a rival disappointed suitor for the company, not a railroad industry participant, and accordingly having a rival takeover proposal free of any Board review.

The Board would have to define the factors that would constitute the public interest at this early stage of the case – accepting what is likely to be the Applicants' narrow concept of the public interest (that is, avoiding a discussion of the merits that only the full Application would present), or rejecting that concept

40 Since the Board's present rules permit a voting trust whenever it meets the generic requirements of Part 1013, the requirement of a demonstration of a "consistency with the public interest" must be addressed to the specific transaction and to be something different from "insulation from control."

and specifying its own. Then it woulu nave to apply its definition of those factors, in a possibly controversial and litigious environment, to the skeletal case before it. That is likely to result in Court of Appeals litigation, without the moorings of the case law that has been decided under the existing arrangements.

Instead of posing cut and dried issues as to whether a voting trust agreement cut from the cloth conventionally tailored in prior transactions provides effective insulation from control, the issues for a reviewing court will be selected by a party challenging the voting trust agreement after the Board has found it consistent with the public interest. Such a party will accuse the Board of making a decision of consistency with the public interest, launching a process which commits, for a lengthy period, a rail carrier to insulation from takeover by another party, and in any event, to sterilization in a voting trust and the possibility of divestiture, on the basis of the flimsiest of evidence of "consistency with the public interest." The issue will not be whether the private parties may go forward — at their peril — but whether a federal agency has made a sustainable finding of consistency with the public interest.

This difficulty is not speculative but is inherent in the circumstances. The Board (or its staff) have in the text of the Voting Trust Agreement the basis for determining whether it provides the proper insulation, assuming the independence of the trustee. The evidence before the Board would not be enough to permit any broader finding to be made, let alone one of "consistency with the public interest," however defined.

The potential of the new rule for doing mischief is very considerable. It increases the handicap of parties within the industry in effecting merger and acquisition transactions with a rail carrier in comparison to those who are outside the industry who seek to control major rail carriers. With many rail stocks at low valuations, if ever there was a time to initiate such a change in policy — and we would question whether there ever would be, for the reasons set forth above — this is not that time. The present rule is not broken and so should not be fixed; and certainly not by a "fix" so flawed itself as this one.

CONCLUSION

The Board has avoided the pitfall of broad reregulation suggested by some in the ANPR process, and the proposed rules promise to increase attention to the competitive impacts of proposed mergers as the Board undertakes its public interest calculus. As demonstrated by nearly two decades of post-Staggers market-driven competition, the Board's choice should preserve the benefits of competition for shippers, the industry and the economy overall. It is important that the Board not allow these benefits to be corrupted by the process and we believe, that in certain respects, the proposed rules do just that. As we demonstrated above, the Board should not leave open a route to reregulation through the back door of merger conditions by creating a system of presumptions against mergers and creating an expectation that certain parties, otherwise unaffected by the merger, will receive various forms of property under the guise of "competitive enhancements." Done on a broad scale, this is nothing more than the reregulation rejected in the first instance. Done on a smaller scale, such an approach is fraught with problems. Such a "merger tax" abandons the Board's precedents, subjecting merger approval to challenges by those not on the receiving end of these handouts. It is also outside the Board's delegated authority, and subjects the entire process to a heightened sense of uncertainty that likely will deter or eliminate procompetitive mergers. Any that develop against this backdrop will be encumbered by a lengthy, complex procedural nightmare as shippers and other railroads vie for the spoils of the process. This makes for bad policy.

The proposed rules are also too rigid in imposing a "snapshot" approach to service assurance and integration planning that will create perverse effects by making it more difficult for applicants to adjust to changing conditions in ways that will benefit shippers overall. One of the primary lessons learned from past integration problems is that conditions change as integration proceeds, and an iterative process enables adjustments to be made that serve the interests of affected parties and affords them the kind of notice that allows them to take advantage of those changes.

Another area where the proposed rules could undermine the Board's goals is in the Board's admonition that negotiation of merger implementation with labor should not override collective bargaining agreements. Like the Board's proposed presumption of harmful competitive effects described above, this collective bargaining presumption is without precedent and will encourage a more protracted and difficult process, the net effect of which is to discourage the negotiated agreements the Board espouses. Finally, proposed changes respecting voting trusts will unnecessarily add to the burdens imposed in mergers between Class I rail carriers, and in any event will greatly prejudice such transactions as against unregulated acquisitions of rail carriers.

Respectfully submitted.

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November 17, 2000

CERTIFICATE OF SERVICE

The undersigned counsel for CSX Corporation and CSX Transportation, Inc. hereby certifies that on this 17th day of November, 2000, a copy of the foregoing "Opening Comments of CSX Corporation and CSX Transportation, Inc.," was served on all parties of record by first-class mail, postage prepaid, or more expedited method.

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